

~~SECRET~~MDAC Fact Sheet # T-5
November 1, 1954BLOC BALANCE OF PAYMENTS WITH FREE WORLDI. Introduction

Between January 1, 1948 and December 31, 1953, considering only recorded trade and shipping accounts, the bloc as a whole showed an annual deficit which was less than \$100 million (in 1950, 1952, and 1953), but reached a peak of \$220 million in 1951. To make the analysis intelligible, however, it is necessary to consider the accounts of the European bloc and of China separately, for at least two reasons:

- a. Mainland China was not overrun completely by the Communists until 1949. Thus, China was not part of the Soviet bloc until about 1950.
- b. Not enough is known about the internal arrangements of the bloc to determine the extent to which trade between the European bloc and China has permitted the transfer of Free World funds in either direction.

Balance of payments data of the Soviet bloc with the Free World must necessarily be viewed with considerable caution. Only part of the requisite data are obtainable directly: The distinction made repeatedly in the discussion below between recorded and unrecorded 1/ transactions must be emphasized. Unrecorded exports and imports have characterized bloc relations with the Free World to a significant extent in the period under consideration. Although estimates of unrecorded transactions are necessarily based on fragmentary intelligence, the indications are that these transactions constitute an appreciable part of the bloc's trade with the Free World.

1/ Unrecorded East-West trade includes all trade between the Free World and the Soviet Bloc that does not appear in the official trade reports of Free World countries as trade with the Bloc. It includes smuggling and other forms of illegal trade, such as the diversion of commodities to the Soviet Bloc in violation or evasion of Free World controls.

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The reduction in the current accounts deficit reflects primarily:

1. A reduction in Finnish reparations payments from \$20 million a year in 1948-1949 to \$44 million a year in 1950-1952 and to nothing in 1953.
2. The stopping of deliveries under the Swedish-Soviet loan agreement, beginning in 1953.
3. The apparent depletion of foreign exchange holdings, particularly in 1949, 1951 and 1953.
4. Reductions in private remittances from the U.S.
5. The increase in unrecorded imports.

Receipts on capital account have been within \$20 million of the deficit on current account in all years except 1949 and 1953 when they were, respectively, \$117 million and \$100 million less. Except for these two years, these differences could be accounted for largely by changes in net dollar and continental European currency holdings.

Although changes in sterling balances, unrecorded trade and service transactions (both imports and exports), and gold sales have not been considered in this discussion, the data given above suggest that except in 1949 these three factors must have roughly offset each other from a balance of payments point of view.

Data on changes in sterling balances held by the bloc are not available, however, they are believed to be relatively unimportant. Gold sales of about \$100 million per year in 1950-51, of \$16 million in 1952 and of \$147 million in 1953 have been reported by reliable sources. Although there are no grounds to suppose that there were gold sales in 1948, about \$100 million in gold may have moved in 1949. These data suggest that the European bloc could have financed unreported transactions at least equal to their gold sales in 1950, 1951, 1952. In 1949, however, sales of gold were probably caused by general balance of payments difficulties.

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II The Balance of Payments of the European Soviet Bloc With the Free World

In the period January 1948 through December 1953, the balance of payments of the European Soviet bloc showed the following:

- a. There were deficits on trade account every year. Both imports and exports declined during this period, with imports declining faster than exports. The movement has thus been toward balance.
- b. The estimated deficit on shipping account has tended to decline since 1949.
- c. The over-all trade and shipping accounts, although showing a deficit every year, moved toward balance.
- d. The receipts on capital account have been within \$20 million of the deficit each year except in 1949, when they were \$117 million less, and in 1953 when there were \$100 million less.
- e. In every year except 1949, the magnitude of gold sales was much larger than the over-all European bloc balance of payments deficits, which suggests that the surplus proceeds of these gold sales could have been used to finance unreported trade. The decline in capital account surpluses noted in 1953, suggests that gold sales represent the principal source for financing unrecorded imports and trade and shipping deficits.

Exports of the European bloc declined from about \$1,400 million in 1948 to approximately \$1,000 million in 1953. In the same period imports dropped from about \$1,500 million to about \$1,100 million. Thus imports dropped about \$400 million and exports dropped a similar amount.

The over-all trade and shipping accounts of the European bloc showed an average deficit of \$191 million in 1948-1949, \$83 million in 1950-52, and \$105 million in 1953.

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The role Switzerland plays in Soviet gold sales is not definitely known. Zurich is one of the largest gold markets in Europe but, until 15 May 1954, trading was restricted by a 4% tax on all gold bought for retention in Switzerland. The Union Bank of Switzerland is believed to have an agreement with Samuel Montagu and Company of London on gold purchases from the Soviets.^{6/} One Soviet shipment was reported to have been received directly at the Union Bank in Zurich from Prague.^{1/}

The overall policy implications of the increased flow of Soviet gold during the past year can only be conjectured. It is likely that the USSR needed foreign exchange, especially sterling, to finance a trade imbalance in 1953 and 1954. Such an imbalance existed in 1953. There remains the possibility that the USSR is building cash balances in western banks for other undisclosed purposes. When the 1954 Bloc-West balances of trade and payments are known, this possibility can be checked.

The greatest volume of gold trading is done with standard bars, i.e. bars weighing 12.5 kilograms and 995/1000 fine.^{3/} Soviet gold bars meet these requirements for quality and thereby qualify as "good delivery." The seals of a group of refiners immediately qualifies their bars for delivery as fulfillment of contracts and the stamp of the Moscow refinery is included in this group.

It cannot be conclusively stated, however, that all Soviet gold is shipped in standard bars nor that it bears the mark of the hammer and sickle. Gold is carried in Soviet diplomatic pouches, undoubtedly in less than 12.5 kilogram bars. Shipments of Soviet bars weighing one kilogram and not bearing the Soviet emblem were purportedly received in Paris.^{2/} It is quite likely that the standard bars upon their receipt in Amsterdam, were remolded into the small one kilogram bars and the telltale mark of the hammer and sickle removed. This is one factor that makes the tracing of Soviet gold sales so difficult.

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Almost all international precious metal shipments move by air since the insurance costs on gold shipments vary directly with the number of days it is in transit. Available reports indicate the route is generally from Moscow and Prague to London or Paris or Zurich, frequently via Amsterdam. Some shipments have moved from the USSR to points in Scandinavia where transhipment was made to London.

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III Communist China's Balance of Payments With the Free World

Historically, China's balance of payments has been characterized by a large deficit on trade and services account which was filled by personal and institutional remittances from overseas Chinese. A similar pattern is shown by Communist China's balance of payments with the Western world, although a number of important changes have taken place. In brief, the situation was as follows:

1. In 1946-1948, before the Communists seized control, China showed an average annual deficit of \$570 million on current account. This was financed by UNRRA and U.S. grant and loan aid which averaged \$370 million, by private remittances, which averaged \$115 million, and by the sale of securities and short-term foreign assets, which averaged \$65 million.
2. Data for 1949 are not available because of the confusion attendant upon the Chinese Communist advance.
3. The cumulative balance on recorded trade and shipping account from January 1, 1950 through December 31, 1953 shows a deficit of \$90 million. Unrecorded imports totaled \$250 million from 1951 through 1953; they probably were not important until 1951, since the imposition of Western security controls did not take place until the end of 1950. The principal source of funds for financing this import surplus was remittances from overseas Chinese. Other sources were Hong Kong dollars, U.S. dollars, clandestine exports of narcotics, and possible gold and silver collected from domestic hoards.

The balance of payments of China with the Free World, considering only recorded trade, is shown in the following table:

Balance of Payments of Continental China With the Free World
(In millions of U.S. dollars)

	1948 a/	1950	1951	1952	1953	Cumulative (1950-53)
Exports (f.o.b.)	248	400	317	270	322	1,309
Imports (f.o.b.)	-456	-393	-420	-237	-263	-1,315
Shipping (on imports	-36	-21	-36	-13	-16	-86
Balance on Trade and Shipping	-244	-14	-139	20	43	-90

a/ Total trade of China. Trade with the Soviet bloc was insignificant in 1948.

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BLOC BALANCE OF PAYMENTS WITH FREE WORLD

SOURCES:

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The Balance of Payments of the Soviet Bloc with the Free World, 1948-1953.
November 1954.

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November 1, 1954SOVIET GOLD SHIPMENTS

The level of Soviet gold shipments during the first five months of 1954 indicated a continuation of the heavy sales begun in late 1953. Shipments for January through May were estimated at 95 to 125 million dollars. Beginning in June and continuing through September reports indicated a slowing down of Soviet gold shipments. Shipments to United Kingdom appeared to have stopped completely. France received a shipment of approximately 2 million dollars in June. An unconfirmed shipment of 42 million dollars in September went to three Scandinavian countries - Sweden, Norway and Denmark. Thus, for the nine month period, January through September, Soviet gold sales are estimated to have been between 98 and 167 million dollars.*

In the United Kingdom, most sales of Soviet gold were presumed to have been made direct to the Bank of England. After 22 March when the London Gold Market reopened, Soviet gold was reported to have appeared there. In late 1953 and early 1954 Soviet gold is known to have been flown directly from Moscow to London.

It is not certain who in France has been the purchaser of Soviet gold. French gold imports from the USSR were obtained from official statistics and therefore yield no clue as to the buyer. Various reports, including French newspapers, indicate the sales were to the Exchange Stabilization Fund and that the gold would probably be applied against the French debt to the EPU. To an unknown extent, the sales may be attributed to Soviet desire for transferable sterling which was

* Possible sales through the Near and Far Eastern markets are not included in the above computations nor was an unconfirmed report that mentioned a 10 ton shipment of Soviet gold to the Tangier market.

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obtainable in France. ^{1/} The Paris market, probably the largest on the continent, is thought to have received Soviet gold directly from Iron Curtain countries or by way of Amsterdam. It is legal for gold to be traded in France provided it has been "residing" within that country. It is illegal for the metal to be imported or exported without a permit, which is rarely granted. Thus, the market depends greatly on smuggling from areas where gold is freely traded.^{2/} Gold, of possible Soviet origin, is known to be smuggled from Switzerland to France with the full knowledge and tacit approval of the Swiss and French government. Smuggled gold would not enter into French official statistics.

Concerning the Soviet sales of gold to Scandinavian countries, the following reasons may be proffered:

1. The USSR has had continuing unfavorable trade balances with these countries and was undoubtedly being pressed for settlement;
2. Substantial postwar Swedish sales to the USSR were financed with a Swedish loan and when this was exhausted, other means of financing had to be found if exports to the USSR were to be continued. The fact that Danish Minister of Labor and Commerce, J. O. Krag, stated early this year that Denmark was willing to purchase Soviet gold lends confirmation to the reported Scandinavian receipts. ^{3/}

In addition to the gold estimated to have been shipped to the West, the USSR concluded agreements for repayments of claims with two other free world countries, Finland and Iran. The agreement with Finland provided for a gold payment in partial settlement of the 1954 Finnish trade credit. The agreement was implemented on 8 June with the arrival of gold valued at about 5 million dollars. ^{4/} On 1 July, the Soviets agreed to pay eleven tons of gold valued at approximately 12 million dollars to Iran in partial settlement of claims arising from wartime occupation of the country by the Soviet army. ^{5/}

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The best unofficial U.S. estimates of the Chinese Communist foreign exchange position from January 1, 1951 to December 31, 1953 is summarized in the following table:

Estimated Sources and Uses of Foreign Exchange of Communist China - Cumulative from January 1, 1951 through December 31, 1953
 (in millions of U.S. dollars)

	<u>Sources</u>		<u>Uses</u>
Remittances	275	Balance on recorded trade and shipping	75
Sale of Hong Kong and U.S. currency	20	Unrecorded imports	200
Reduction of other foreign exchange balances	30		
Total sources	325	Total uses	325

It should be emphasized that these estimates are based on a wide range of possibilities, and, except for the balance on recorded trade and shipping, do not have a basis in reliable statistics.

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3. State, Despatch #1059, Copenhagen, 26 March 1954, C.

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